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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1958

No. 310

BOSTON AND MAINE RAILROAD; THE NEW YORK, NEW HAVEN AND HARTFORD RAILROAD COMPANY; THE NEW JERSEY AND NEW YORK RAILROAD COMPANY, HORACE BANTA, Trustee; THE LONG ISLAND RAIL ROAD COMPANY,

Appellants,

against

UNITED STATES OF AMERICA; INTERSTATE COMMERCE COMMISSION *et al.*,

Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF MASSACHUSETTS.

SUPPLEMENT TO APPENDIX A TO JURISDICTIONAL STATEMENT

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INTERSTATE COMMERCE COMMISSION

No. 31358

CHICAGO, BURLINGTON & QUINCY RAILROAD COMPANY ET AL.

v.

NEW YORK, SUSQUEHANNA & WESTERN RAILROAD COMPANY ET AL.

Decided October 17, 1955.

Per diem charges of $1.75, $2, and $2.40 for the use of railroad-owned freight cars when on the lines of rail carriers other than their owners, found not in excess of reasonable compensation. Proceeding discontinued.

S. R. Brittingham, Jr., R. R. Bongartz, Carson L. Taylor, J. P. Fishwick, L. J. Huegel, F. E. Baukhages, C. C. Howell, R. B. Gwathmey, E. H. Burgess, D. O. Mathews, Eldon Martin, Edwin C. Matthias, D. S. Wright, B. J. Viviano, Thomas T. Railey, H. Merle Mulloy, J. L. Homire, Seddon G. Boxley, J. T. Suggs, W. C. Plunkett, E. S. Davis, J. H. Miller, J. L. Rice, A. C. Scott, R. S. Outlaw, J. H. Wright, E. J. Zoll, Jr.,

J. Carter Fort, Jr., Alfred W. Hesse, Jr., Martin A. Meyer, Jr., and *George W. Holmes* for complainants.

Hewitt Biaett, J. C. Kauffman, David L. Farley, Jr., Ross L. Thorfinnson, W. H. Parsons, Prime F. Osborn, III, Thormund A. Miller, M. C. Smith, Jr., Robert D. Brooks, John Colgren, Kemper A. Dobbins, Warren H. Ploeger, W. H. Fitzpatrick, John F. Reilly, Paul F. Robinson, Martin L. Cassell, Eaton Adams, Francis J. Melia, D. D. Dart, M. L. Countryman, Jr., Matthew Crawford, and *Milton Ferguson* for interveners in support of complainants.

Carl E. Newton, Granville Whittlesey, Jr., W. J. Hickey, J. M. Hood, J. W. Grady, W. J. Myskowski, H. D. Boynton, Richard Jackson, Lawrence Chaffee, William A. Colton, Richard Swan Buell, and *Joseph P. Hawryluk* for defendants.

W. J. Hickey for interveners in support of defendants.

REPORT OF THE COMMISSION

BY THE COMMISSION:

Exceptions to the report proposed by the examiner, and replies thereto, were filed by the parties, except interveners listed in the footnote.[1] We have heard oral argument. Our conclusions differ in part from those of the examiner. Exceptions and requested findings not specifically discussed

[1] The following carriers intervened in support of the complainants but did not join in their exceptions: Erie Railroad Company, Minneapolis, St. Paul and Sault Ste. Marie Railroad Company, Southern Pacific Company, Texas and New Orleans Railroad Company, Western Maryland Railway Company, and The Pittsburgh & Shawmut Railroad Company.

in this report nor reflected in our findings or conclusions have been considered and found not justified.

This complaint was filed on September 21, 1953, by 19 of the larger class-I railroads.[2] The defendants include, among others, 5 class-I railroads: Boston and Maine Railroad; The Long Island Railroad Company (William Wyer, Trustee), called the Long Island; The New York, New Haven and Hartford Railroad Company, called the New Haven; New York, Susquehanna & Western Railroad Company, called the Susquehanna; and Rutland Railway Corporation. Six short-line railroads are also defendants: Atlantic & East Carolina Railway Company; Barre and Chelsea Railroad Company; East Tennessee and Western North Carolina Railroad Company; St. Johnsbury & Lamoille County Railroad; The New Jersey and New York Railroad Company (Horace Banta, Trustee); and Mississippi & Skuna Valley Railroad Company. The last-named defendant is a class-III railroad; the preceding 5 are class-II lines.

There are 15 interveners in behalf of the complainants, all of them being class-I railroads. The interveners in be-

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[2] The Atchison, Topeka and Santa Fe Railway Company, Atlantic Coast Line Railroad Company, The Baltimore and Ohio Railroad Company, Chicago & Eastern Illinois Railroad Company, Chicago, Burlington & Quincy Railroad Company, Chicago, Milwaukee, St. Paul & Pacific Railroad Company, Great Northern Railway Company, Gulf, Mobile & Ohio Railroad Company, Illinois Central Railroad Company, Lehigh Valley Railroad Company, Missouri Pacific Railroad Company (Guy A. Thompson, Trustee), Norfolk and Western Railway Company, The Pennsylvania Railroad Company, Reading Company, The St. Louis-San Francisco Railway Company, Southern Railway Company, The Texas and Pacific Railway Company, The Virginian Railway Company, and Wabash Railroad Company.

half of the defendants, 56 in number, are rail carriers principally in classes II and III. All of the interveners are listed in the appendix hereto.

The complaint grows out of a disagreement between the complainants and the defendants concerning the reasonableness of per diem charges for the use of railroad-owned freight cars payable by nonowning railroads. In *Alabama, T. & N. R. Co.* v. *Aberdeen & R. R. Co.*, 274 I.C.C. 383, decided July 11, 1949, hereinafter referred to as the 1949 report, we found that the per diem charge of $1.50 per day then in effect was not shown to be either unreasonably high or unreasonably low. Effective on November 1, 1949, that charge was increased to $1.75 by action of members of the Association of American Railroads, hereinafter called the AAR, under procedure described in the 1949 report.

The procedure for establishing per diem charges was considered by division 2 in *Association of American Railroads—Agreement*, 277 I.C.C. 413, and approved as conforming to section 5a of the Interstate Commerce Act. The report included the following paragraph:

> Articles XI and XII accord to each subscriber certain individual rights. The former states that the agreement shall not be construed to prevent or limit recourse to this Commission by any subscriber for any relief (in pending proceedings, or otherwise) accorded by law in respect of any of the matters covered thereby. The latter (article XII) provides that all subscribers shall have the free and unrestrained right to take independent action either before or after any determination arrived at though the procedure provided for in the agreement.

This agreement became effective on October 7, 1950. Under the procedure which it set up the per diem charge was increased to $2, effective on May 1, 1952, and to $2.40 on August 1, 1953.

The Susquehanna, which was not a party to the agreement, notified the complainants in March 1951 that after April 1 of that year it would refuse to pay the charge of $1.75 but would settle on a graduated scale ranging from $1.20 to $2, depending on the age of the car. In 1953 it offered to increase that scale to a range between $1.33 and $2.21. The complainants refused those offers, and the car rentals payable by the Susquehanna are now involved in a number of pending lawsuits.

In June 1953 the Boston & Maine, the New Haven, and the Rutland gave notice of their refusal to pay the charge of $2.40, as well as the former $2 charge after July 31, 1954. Later, the Boston & Maine offered to pay on a graduated basis or a flat rate of $1.72 per day. The Long Island in August 1953 advised that it was willing to continue paying a $2 charge but would not recognize the $2.40 charge. The Atlantic & East Carolina, St. Johnsbury & Lamoille County, New Jersey & New York, and Barre & Chelsea have followed a similar course. The situation with respect to present payments by the defendants other than those here named is not disclosed.

It is alleged in the complaint that, to the extent that the defendants have paid and are paying or offering to pay charges less than those generally in effect as above indicated, "such payments have been, are and would be unjust, unreasonable and noncompensatory, in violation of para-

graphs (4), (10), and (11) of section 1 of the Act; and such action by defendants has been, is and would be disruptive of the 'uniform national basis' of handling per diem, which has been deemed necessary by the Commission in order to facilitate 'the performance of orderly transportation service by railroad in the public interest.' *Association of American Railroads—Agreement, supra,* 423." The prayer of the complaint is that—

> the Commission find and declare that the per diem rates of $1.75 and $2, during the periods in which these rates were effective, were just, reasonable, and otherwise lawful, that the current per diem rate of $2.40, effective August 1, 1953, is just, reasonable and otherwise lawful, and that the performance of orderly transportation service by railroad in the public interest requires uniform observance of such rates by defendants together with other carriers; and that the Commission grant such other and further relief as may be required in the premises.

The complainants expressly disclaim any intention to invoke the only specific power with respect to per diem which we have, namely, in section 1 (14)(a) of the Interstate Commerce Act to establish "the compensation to be paid and other terms of any contract, agreement, or arrangement for the use of any locomotive, car, or other vehicle not owned by the carrier using it (and whether or not owned by another carrier, * * *." Such action would involve the entry of an order, which presumably would continue in effect for the indefinite future and, unless it were vacated or modified, would render the present procedure for dealing with per diem charges inoperative.

In one of the complaints considered in our 1949 decision, No. 29587, the complainants, which were short-line railroads, asked that we promulgate a formula to be employed in the future in determining the lawful compensation to be paid for the use of railroad-owned freight cars. The pleadings in the instant case raised no such issue.

In a joint answer to the complaint filed by the Boston & Maine, the New Haven, and certain short-line defendants, these parties ask "that the Comimssion find and determine and fix by order the rate or rates for the use of freight cars to be paid by complainants to defendants and by defendants to complainants." The short-line defendants and interveners requested in their briefs that we determine and definitely fix the amount of compensation to be paid by a rail carrier when it uses the freight cars of another, but the briefs of the other defendants were less positive.

The New Haven and the Boston & Maine asked for a declaration that the present per diem rate is unlawful and as a maximum should not be more than $1.04 per day if it is to be fixed as a single amount. Alternatively, they expressed preference for a graduated scale. The Susquehanna asked principally that the graduated scale which it favored be found not unreasonably low or noncompensatory. The Long Island and the New Jersey & New York urged that the complaint be dismissed, and asserted that we are not empowered to prescribe charges for car hire retroactively.

In their exceptions to the proposed report, the defendants generally go beyond the positions taken in their briefs above described, and request that a formula for the determination of per diem charges be prescribed. Under such a formula,

according to one of the defendants, "the carriers would be required to get exact and complete figures and to make the computations themselves, with the right of recourse to the Commission in the event an agreement could not be reached." This contention is outside the scope of the proceeding as developed in the pleadings, and such a disposition would hardly be desirable except in a proceeding to which all rail carriers were parties.

At a prehearing conference it was suggested that findings such as those sought by the complainants might be in the nature of a declaratory order, as authorized by section 5(d) of the Administrative Procedure Act. Later, some of the defendants, as above pointed out, made requests for findings which appeared to be of the same nature. In exceptions to the proposed report, which recommended action under that section, the defendant New Haven questions the applicability of a declaratory order to the present controversy.

The declaratory order is a relatively new administrative remedy, and no definite limits to its use as yet have been set. The power of issuance is committed to the agency "in its sound discretion . . . to terminate a controversy or remove uncertainty." Manifestly, a controversy exists here, and we consider that a declaratory order would be appropriate.

With the exception of our decision in *Increased Per Diem Charge on Freight Cars*, 268 I.C.C. 659, which was set aside on judicial review (*Palmer* v. *United States*, 75 F. Supp. 63), we have never undertaken to establish a general basis of per diem charges under our authority in section 1(14)(a)

of the act, but have considered such charges in a number of cases arising on formal complaints. The present system of rentals in its broad form has been worked out by the railroads themselves. The per diem plan was adopted in 1902 after a mileage system was found to be unsatisfactory for reasons mentioned in *Rules for Car-Hire Settlement,* 160 I.C.C. 369, 375. The charge has been uniform for all types of freight cars, and up to the time of the present controversy it has applied uniformly to all railroads, subject to the operation of reclaims. In our 1949 report (page 386), we said:

> For many years the per diem rate has been based on average costs. The daily rental for a car valued at $2,000, for example, is the same as that for a car worth twice as much. There is no request herein for different per diem rates on freight cars of different ages, sizes, or classes. A carrier which has a foreign railroad car on its rails immediately after midnight pays the rental for that calendar day in the absence of some special agreement. If it receives a car in interchange after midnight and delivers it in interchange before the following midnight, it does not pay any car rental.

Some of the defendants here question the principle of uniformity and introduce evidence in support of their views. These will be discussed before the main issues in the case are considered.

Both the Long Island and the New Jersey & New York, whose lines are partly in the metropolitan area of New York City, perform comparatively short line hauls in their freight service. The average detention per car in their

terminals is high. These defendants believe that the basis of per diem charges should take into account a distinction between items of car-ownership cost attributable to movement use (mileage) and those related to the passage of time. They therefore suggest a basis under which "each using road would pay time costs in proportion to the time that it holds the car and mileage costs in proportion to its own mileage use of the car."

Unless we dismiss the complaint, the Long Island and the New Jersey & New York urge that we

> (a) undertake to determine true freight car ownership costs * * *; (b) make an accurate separation of such costs between time and mileage; (c) determine separate average unit costs for time and mileage; and
>
> (d) fix separate car hire charges for each user road reflecting the average time and mileage costs for which such road is responsible.

Admittedly, such a determination could not be made from the evidence in this case; moreover, it would involve a long and complicated statistical undertaking. If by that means a scheme of equitable separate charges for individual user roads could be devised, there would be an increase in the labor now required for settling per diem accounts.

The New Haven and the Boston & Maine suggest a plan of per diem charges under which there would be a variation of rates with respect to owner railroads based on the average age of their cars. The Susquehanna also supports this suggestion. According to the sponsors, this plan "by giving higher rent for new than for old cars would furnish

an incentive to car owners to renew the fleet and to get rid of old equipment." The steps necessary to carry out the plan are stated as follows:

> Mr. Glacy's program assumed that in each year the AAR would ascertain for each owning railroad the inventory of its cars; ascertain for each group of cars of each railroad the proper charge per day; and derive for each railroad a composite figure which was the weighted average rate per day for its entire fleet. The AAR would then publish a booklet showing each owning railroad's composite rate, which would be the basis.

This plan, too, would necessitate a complicated statistical operation to ascertain the proper composite figure, and it may well be doubted whether the clerical labor required in computing per diem credits would be as simple as the sponsors believe.

As above indicated, the suggested plans for varying per diem charges could not be put into effect without an extensive investigation either by this Commission or by the AAR. The facts and arguments here presented are not persuasive that plans of this kind are desirable.

There is general agreement that car rentals, however established, should be reasonably compensatory and no more. *Palmer* v. *United States*, *supra*, page 69. The determination is basically a problem in cost accounting. The earliest attempt to deal exhaustively with the problem was made 45 years ago by the so-called McCrea Commission, composed of 5 railroad presidents. They adopted the prin-

ciple that the per diem charge should cover repairs, taxes, depreciation, interest on investment, and miscellaneous expense incidental to ownership. This principle has been generally accepted as valid ever since, but there has been continuing controversy as to how it should be applied. Indeed, the members of the McCrea Commission themselves reached three different conclusions on that point.

The principle just referred to serves as a guide for the General Committee of the AAR, which is charged with studying proposals for changes in per diem rates, aided by a subordinate special committee, known as the Subcommittee on Mileage and Per Diem. Costs are allocated to the various categories from expense figures reported to the committees in response to questionnaires sent to car-owning railroads. The General Committee alone decides what proposed changes in the per diem rate shall be recommended to the Board of Directors of the AAR for submission to subscribers to the per diem agreement.

In the 1949 report, we discussed the allocations of costs for 1946 presented in support of the per diem charge of $1.50 there in issue. We criticized some of the allocations as too large, but in respect of other important items we made comments which have been interpreted as finding that those items were understated.

In that report, however, we dismissed the complaint in No. 29587, filed by the short lines, in which we were asked, among other things, "to promulgate a formula to be employed in the future in determining the lawful compensa-

tion to be paid for the use of railroad-owned freight cars." Also, we dismissed the complaint in No. 29751, in which 6 large western rail carriers took the position that the per diem charge of $1.50 was "inadequate, unjust, and noncompensatory."

In this case the complainants seek findings which would approve all per diem charges established after the 1949 report. In each instance the General Committee studied statistics reported by class I railroads in response to questionnaires. Those upon which the charge of $1.75 was based were for 1948, but there was an adjustment to reflect wage rates, material prices, payroll taxes, and other determinable increases up to September 1, 1949.

The statistics pertaining to the $2 charge were those for 1950, projected to include cost levels as of April 1951. Full recognition was thus given to the 40-hour week, which was in effect throughout 1950. The present charge of $2.40 was based on figures for 1952. The information for the latter year was received from 121 railroads, having approximately all the freight-car ownership of class I railroads. Concerning the latest study, the complainants' principal witness asserted that it "came closer to applying the Commission formula [1949 report] than any of its previous studies leading to a per diem adjustment."

Freight car repairs. This is the largest single category of expense included in the per diem charge and amounts to about 40 per cent of the total. Also, it is used as a basis of allocating certain other costs. The basic figures for this

item are derived from account 314, Freight Train Cars—Repairs, in the accounting classification. The reported total for 1952 was $586,914,603. To this the General Committee added $24,965,504 for switching home freight cars marked for repairs, and deducted $65,887,034 for costs of car users' repairs to foreign cars damaged by them through improper handling, compensation for foreign cars destroyed on car users' lines, certain switching costs, and a portion of labor costs of inspection and other service at terminal junction points. The reasons for these adjustments were stated on pages 390 and 391 of the 1949 report. The complainants thus estimate the cost of repairs at 97.836 cents per active car-day.

In the 1949 report we found that there should have been a further deduction of the costs incurred by car users for inspection of foreign cars not charged back to car owners. Applied to the 1952 study, the deduction would amount to only about 5 cents per day, a relatively small figure. The complainants have not seen fit to consider this deduction as a part of what they regard as our formula, approved or prescribed in the 1949 report. They argue:

> It is technically true that the expense is not one which the owner bears immediately and directly but it is one which the owner bears vicariously and by substitution; and nonowners should not be shielded from the impact of this ownership burden.

The defendants contend that there should be even larger deductions for the expense of car inspection now included

in account 314. Some of the defendants would eliminate all inspection costs on the ground, as stated by one of them, that "inspection is obviously primarily for purposes of operation and safety, and with the primary objective of preventing breakdowns in transportation on the inspecting line, which is the line which is using the cars." Such a sweeping generalization can not be sustained. The instructions published in connection with the accounting classification direct that "the cost of repairs * * * shall include the cost of inspecting to determine the repairs necessary and * * * the cost of inspecting and testing after repairs have been made * * * to determine whether the repairs have been properly made." The cost witness for the short-line parties in effect conceded that inspection costs of this kind may properly be considered maintenance. If there is to be any segregation of inspection costs as between maintenance and transportation, it should follow an authoritative study.

In the 1949 report we said (page 391):

> Numerous repairs are applied to freight cars when on the lines of railroads other than their owners, and, except for the relatively few due to defects for which the using line is responsible by reason of improper handling, commonly called no-bill repairs, definite sums published in connection with the freight-car interchange rules may be billed against and collected from the owning railroads. Such amounts are revised from time to time, to correspond with changes in labor and material costs, but as the published revisions lag behind changes

in price levels, the actual costs, in a period of rising prices, of supplying materials and applying repairs to foreign cars may, and frequently do, exceed the amounts that may be recovered.

Some of the defendants contend that losses which they and other carriers incur because of their inability to recoup full costs of these repairs, both on foreign per diem cars and on mileage cars, should be deducted from the total car-repair costs. It is testified for the Boston & Maine that this deficiency is equivalent to nearly 30 per cent of its charges to account 314, and applying this percentage to aggregate car-repair costs of $586,914,603 used in the complainant's study, it suggests the elimination of $175,006,186 from that aggregate. It would be very hazardous to make any such adjustment in the absence of fairly complete information bearing on this suggestion. Other defendants more cautiously suggest only that the situation should be investigated. This attitude seems to be reflected in the recommendation of the Susquehanna that "there should be segregated and eliminated from ownership cost figures all amounts spent by users for the maintenance of cars which are not recoverable by the user from the owner."

The various defendants introduced four cost studies in which the aggregate car-repair figures there shown differ widely. That of the short-line parteis shows a total of $498,922,522. The figure in the New Haven study is $457,610,831. Much lower are those of the Boston & Maine, $259,486,694, and of the Susquehanna, $217,158,403. Each

of the witnesses who presented these studies is a man of long experience in this field. The wide variations in these figures apparently reflect individual differences in respect of reliance upon conjectural factual data.

Some conjecture of this kind is inescapable because of the comprehensive nature of account 314. It is the largest of the primary operating expense accounts, embracing nearly 10 per cent of total freight expense. It includes "the net loss sustained on account of the destruction of foreign cars" and "amounts paid to others for repairs of freight cars for which the carrier is liable." Among the freight cars covered by the account are cabooses and refrigerator cars. As of November 1, 1953, however, 96.5 per cent of the cars owned by class I carriers consisted of box, gondola, hopper, stock, and flat cars, subject to per diem.

The Subcommittee on Mileage and Per Diem, in 1951, came to the conclusion that a proper diem charge could be more readily determined if account 314 could be subdivided, and recommended that all the railroads do so beginning with 1952. The Subcommittee found that there was "considerable variation in the practices of various railroads in the charging of inspection costs as between account 314 and account 402." It was of the view that "it would be better if car repairs for cabooses could be eliminated from account 314 and caboose-car days eliminated from the freight-car day divisor." The Subcommittee also proposed that there be a separation of repair costs for home cars, foreign cars, and railroad and privately-owned mileage

cars, as well as cabooses, and a separate showing of cost of classified repairs, running repairs, switching expenses, and credits for sales of scrap. The General Committee disapproved this recommendation because of the additional expense which would be required for such detailed accounting.

The recommendation of the Subcommittee deserves further consideration. However, it is not desirable to delay the decision of this case pending an effort to provide additional data bearing on car repairs. Accordingly, we conclude that car-repair costs should be determined in the manner specified in the 1949 report.

Taxes.—In 1952, the class I railroads showed a total investment of $32,698,240,806 in property, material, and supplies, upon which they paid property taxes (personal and real), and other taxes in lieu thereof, but excluding State income taxes, amounting to $319,221,322, a ratio of 0.976 per cent. That ratio is applied to ledger value of freight cars, undepreciated, and a freight-car repair proportion of ledger value, undepreciated, of shops, enginehouses, et cetera, producing $56,639,614. To this figure was added $23,354,062 as a proper estimated share of payroll taxes, which makes a total of $79,993,676 for taxes. This is translated into a figure of 14.334 cents per active car-day for taxes.

The defendants point out that in some States no ad valorem taxes are levied on freight cars, and makes certain other criticisms of the complainants' tax allocations. The

Susquehanna suggests that the figure of 14.334 cents "should be reduced by at least 50% pending a country-wide analysis leading to calculations based on accurate comprehensive figures." The reduction would amount to 7 cents per active car-day. The Boston & Maine is of opinion that in the light of its experience the property-tax figure of $56,639,614 should be reduced by 70 per cent, making it $16,991,884.

Considering the record as a whole, the complainants' allocation of this expense does not appear to be excessive.

Depreciation. This is the second predominating element of expense in the per diem charge. The wide difference of opinion among the parties as to what constitutes a proper basis for annual depreciation charges which properly should be included in the per diem rate continues to exist substantially as we noted in the 1949 report, at page 392. We there observed:

> There is a difference of opinion among carrier representatives as to whether annual depreciation, to be included in the per diem rate, should reflect a figure calculated to return to car owners the same number of dollars per car as originally were invested, or whether the amounts should be sufficient to enable a car owner at retirement to purchase a new car of like kind and size at the then current price level, which might be, and at the present time is, much higher than the price levels prevailing when many of the cars now in service were constructed.

That question was resolved together with the closely-related element of interest return, when we stated in the 1949 report as follows:

> Carriers who now buy cars must pay prices predicated on present values, and those who rent cars owned by others should expect to pay rentals based on such values.

Thus, both interest and depreciation, excepting a minor item of depreciation on fixed facilities, were calculated on the basis of reproduction cost for the purposes of determining a reasonable per diem charge in the 1949 proceeding.

Reviewing the matter for the purposes of this proceeding we note from the evidence now before us that the present day prices are still well above the levels of an era when many of the cars were purchased. Data of record show a range of freight-car prices from 1938 to 1952, from $2,569 to $5,859 for box cars and $2,278 to $5,814 for gondola and hopper cars.

A witness for the short-lines expressed the opinion that depreciation based on cost of reproduction was not in accord with governmental regulations or recognized accounting practice. That opinion is supported by some accountants and economists who believe that the purpose of depreciation accounting is not to provide a fund for the replacement of units of property being retired, but rather to recover the cost of those units in current use. In their exceptions to the proposed report, the complainants and the interveners which support them put much emphasis on

the views of a group of recent writers in the field of public utility regulation which "recognizes the unreality of original cost valuation and believes that something should be done about it." Some of these writers have suggested or advocated a basis sometimes called economic or value depreciation.

In *United Railways* v. *West*, 280 U.S. 234, cited in our 1949 report, the Supreme Court held that an allowance for annual depreciation should be based on present value and not on cost. That decision was overruled by the Court in *Federal Power Com.* v. *Hope Natural Gas Co.*, 320 U.S. 591, commonly referred to as the *Hope* case. Shortly after the earlier decision we had occasion to consider the question in *Telephone and Railroad Depreciation Charges*, 177 I.C.C. 351, 372-382. There the rail carriers urged "that the operating expense resulting from the retirement of a unit of property is not its original cost but rather the cost of replacing it in kind." Our comments, at pages 377 and 378, were as follows:

> When depreciation accounting is employed, a further and important objection to the cost of replacement or present value method is that retirement and replacement of the unit do not occur when the depreciation charge is made, and may not occur until many years in the future. If depreciation charges, therefore, are made each year on the basis of the current replacement cost or present value, they may prove to be quite out of line with this cost or value at the time when retirement

actually takes place. In view of the constant shift in such costs and values, this would indeed normally be the case, with the result that the depreciation reserve would be either too large or too small. No very satisfactory method of adjusting these irregularities has been suggested. It would also be necessary for us to exercise constant supervision over the depreciation charges, for the determination of current replacement cost or present value is so controversial a matter that it could not safely be left to the discretion of the carriers.

We realize that in determining depreciation the prevailing accounting practice is to use the ledger value, and we are not here concerned with the propriety of that practice. Our problem here is to determine the justness and reasonableness of the per diem rates in effect during the respective periods referred to and at present. In reaching such a determination we would be less than realistic if we failed to take into consideration, as pointed out in the 1949 report, that carriers who now buy cars must pay prices predicated on present values, and those who rent cars owned by others should expect to pay rentals based on such values. Failure to do so would cast an undue burden upon the car owners and favor unduly those who pay rentals.

In a special study such as is involved here we may consider the annual depreciation charges on freight cars for any given year, say 1952, which result from a normal application of the average prescribed rate to undepreciated

ledger value, and also bear in mind the replacement cost level. A ready device or tool for use in measuring the shortcomings of normal depreciation charges, from the standpoint of replacement, exists in our own reproduction cost new figure at the 1952 spot price level. These figures, which are of record, show an index relation of the reproduction cost new value of freight cars as of December 31, 1952, $9,587,048,000 (replacement in kind), to ledger value, $5,416,305,351 (original cost), of 177. We may apply this ratio to the normal depreciation charges to bring them up to that level, which would embrace replacement considerations, or we may simply apply the average depreciation rate to the reproduction cost new value with, of course, the same result. Applying the 1952 average depreciation rate of 3.12 per cent to the reproduction cost new total of $9,587,048,000 results in depreciation charges of $299,115,898.

For the foregoing reasons, we are persuaded that in determining depreciation to be considered in passing upon the compensatory character of per diem charges, the basis should be the undepreciated reproduction value.

Capital charges.—With respect to this element, also, the use of cost and reproduction is in controversy. In our 1949 report (page 393) we said:

> The short line complainants contend that any interest charge on the value of freight cars, repair shops, et cetera, should be based on depreciated ledger cost. Certain other carriers urge the use of depreciated reproduction cost new, termed present value, and in-

> clusion in the per diem rate of interest charges reflecting a rate of 6 per cent. * * * Inclusion in the per diem rate of an interest charge of 6 per cent on average present value of freight cars, freight repair shops, et cetera, does not appear to be excessive, in view of the fact that a portion of the resulting revenue must be paid out as income taxes.

In their brief, the complainants say:

> In connection with the $2.40 rate the General Committee's averaging method produced an interest on value item for freight cars of 43.588 cents, as against 31.516 cents on depreciated ledger value alone. If the General Committee had followed the Commission's decision [1949 report] and used depreciated reproduction value, the amount included in the per diem computation for interest on freight car value would have been 55.660 cents, and the current rate would be substantially in excess of $2.40.

The "averaging method" above mentioned produced an investment base which was the average of depreciated cost of reproduction and depreciated ledger value. To this base a 6-per cent rate of return was applied. The theory followed in determining this base is essentially the same as that of "fair value", which flourished about 25 years ago. In the *Hope* case and others the Supreme Court pointed out that there are various permissible ways in which any rate base on which the return is computed may be arrived at, and that the result reached rather than the method employed is controlling.

The choice of a percentage figure to be applied to the investment base is a point of much controversy. Although all of the defendants take substantially the same position as the Boston & Maine, which asserts that "it would be improper to include anything in the rent base beyond the costs of financing such property—in this instance the interest burden upon a car owner arising out of his acquisition and ownership of a freight car," the only ones making definite recommendations as to a rate of return are the New Haven, the Boston & Maine, and the Susquehanna. The first-named suggests 6 per cent based on ledger value, while the latter two carriers contend that the basis used should be about 4.6 per cent of that value. The latter figure is the result of an averaging process, reflecting, among other things, the average interest rate of 2.39 per cent on outstanding equipment-trust obligations. The complainants stress "risk of ownership" and "burden of replacement" incurred by the car-owning carriers, and hint at the danger to the national economy if railroads which have heretofore been willing to sink capital in freight cars should decide that in view of high replacement costs, prudence no longer permitted them to contribute their part to the national car fleet, but that they should become car renters rather than car owners.

An intervener, The Chesapeake and Ohio Railway Company, which owns a large number of cars and is consequently one of the principal per diem credit railroads, is more specific. It states:

> If the railroads in general, and the Chesapeake and Ohio in particular, are to own the number of cars required by the national economy, the per diem rate must provide adequate compensation after income taxes. If the per diem rate provided a realistic rate of return after income taxes, the railroads, including the Chesapeake and Ohio, would own a larger number of cars and could, in fact, justify increasing rather than reducing their car ownership.

This intervener, therefore, believes that, far from being reduced, the prevailing per diem rate of $2.40 per car per day is at least 97 cents too low and should be increased. The further expansion of the 97-cent figure which it suggests would be accomplished by adjustment of the car-day divisor to be discussed later.

Argument over investment base and percentage rate of return should not obscure the practical point involved, which is the number of dollars available by way of rental to a carrier which makes an investment in freight cars for joint use in nationwide transportation service. It seems clear that the car-owning carrier is entitled to a return larger than one based solely on cost of money measured by current interest rates, for in acquiring cars it acts somewhat as an entrepreneur. It must assume the burden of planning and financing the new equipment in the light of an uncertain demand for cars in general or those of a particular size and type due to unpredictable factors affecting the outlook for rail transportation. In other words, in determining a fair per diem charge some consideration

should be given to what are termed incentive and risk, and an appropriate place for such an element is in the capital charge.

In our 1949 report we stated that an interest charge of 6 per cent of present value of freight cars did not appear to be excessive. We adhere to that view on the instant record.

The car-day divisor.—For reasons which are well-known, it is generally agreed that surplus and unserviceable cars should be excluded in computing average costs per car-day. However, since per diem charges are established for future application, the extent of that exclusion necessarily rests upon an estimate as to the aggregate number of freight cars which the railroads will own in an indefinite future period, the number which will be unserviceable, and the number which will be idle because of insufficient traffic for their full utilization. The last element, which is closely related to fluctuations in the business cycle, is particularly speculative. In the past, average figures for various periods of years have been used in determining the car-day divisor, but other plans have also been considered. After discussing some of those plans at page 389 of our 1949 report, we said:

> The evidence is persuasive that an active-car divisor reflecting average age, now approximating 20 years, of freight cars in service, and covering representative periods of both heavy and light traffic, would produce more accurate results than a period of 5, 10, or 15 years.

It does not appear that theretofore the railroads had ever considered using a period as long as 20 years for this

purpose. In the studies upon which the charge of $1.50 approved in our 1949 decision was based, a 10-year period, 1936 to 1945, was used, and the ratio so arrived at was 86.15 per cent. The 20-year period suggested in the 1949 report covered 1927 to 1946, and produced a ratio of 80 per cent. In the studies which led to the $1.75 charge a period of 15 years, 1934 to 1948, was used to arrive at a ratio of 86.12 per cent. Originally, in the next studies relating to the $2 charge, a 15-year period, 1936 to 1950, was used, and the resulting ratio was 89.13 per cent. However, the General Committee considered it advisable to use the 20 years, 1931 to 1950, and thereby reduce the ratio to 82.75 per cent, incidentally increasing the estimated cost by about 15 cents a day. In the studies on which the present charge was based, a 20-year period, 1933 to 1952, was used, giving a ratio of 86.05 per cent.

In contrast to the foregoing ratios of 86.12, 82.75, and 86.05 are the following actual ratios for the years shown:

Year	*Per cent*
1949	90.39
1950	91.34
1951	94.27
1952	93.59

From 1933 to and including 1940, the average annual ownership of cars by class I railroads was 1,806,065. Because of depressed industrial activity, there were large numbers of surplus cars, and the percentage of unserviceability ranged from 8.8 to 15. The car-utilization ratio

consequently ranged from 63.98 per cent in 1933 to 84.16 per cent in 1940. From 1941 to 1952, inclusive, the class I railroads' annual ownership of cars averaged 1,738,696. Because of the greater average capacity of the cars, increased train speeds, and other means of greater efficiency, including a reduction in the percentage of unserviceability, which ranged from 2.7 to 6.9 per cent, those carriers were able to carry the heavy traffic of the war and post-war periods. Car surpluses after 1940 were negligible in comparison with those of the earlier period.[3] The car-utilization ratio, therefore, between 1941 and 1952 ranged from 90.39 to 96.67. In 1952, the latest year for which figures are of record, the ratio was 93.59. The average for the 5 years, 1948 to 1952, was 92.82, and the average for the 15-year period up to and including 1952 was 91.05 per cent. Taking note of the decline in railroad traffic in 1953 and 1954, the examiner in his proposed report suggested the use of a ratio of 90 per cent as representative of current conditions, subject to verification by actual figures for those years. The complainants in their exceptions do not question the accuracy of the 90-per cent ratio, although they contend that it would be more reasonable to apply a ratio of 86 per cent.

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[3] Complainants show that maximum freight-car surpluses in 1933 to 1940 ranged from 190,370 on March 14, 1940 to 691,587 on January 31, 1933. Minimum surpluses in the same period ranged from 64,299 on October 14, 1939 to 385,137 on October 31, 1933. In the period 1941 to 1952, maximum surpluses ranged from 23,416 on October 20, 1945 to 207,627 on November 5, 1949, and minimum surpluses from 673 on October 23, 1948 to 38,511 on October 4, 1941.

Upon consideration of the matter of the car-day divisor in the light of present evidence, we affirm the finding in the 1949 report that a 20-year period would produce more accurate results than a shorter period. The record does not afford a 20-year experience of car use prior to 1948; accordingly, a 15-year period will be used up to and including that year. We conclude that, for the purpose of determining the compensatory character of the respective per diem charges here under investigation, the reasonable car-day divisors to be used are 86.12 per cent for the 15-year period 1934 to 1948, 82.75 per cent for the 20-year period 1931 to 1950, and 86.05 per cent for the 20-year period 1933 to 1952.

Conclusions.—In accordance with the foregoing views, the figures submitted by the complainants have been adjusted or modified in the following respects: (1) The items representing freight-car repairs and the allocations based thereon are treated in the same manner as corresponding items were treated in the 1949 report, which eliminates certain costs incurred by car-users covering inspection of foreign cars not charged back to the car-owners; (2) depreciation for freight cars is based on undepreciated reproduction value; (3) depreciation for fixed facilities, such as shops, enginehouses, and power plants, a relatively minor item, is based on undepreciated ledger value; (4) return on investment in freight cars, shops, enginehouses, power plants, et cetera, is based on 6 per cent of depreciated reproduction value; and (5) the car-day divisor is based on car-utilization ratios for the respective periods as above noted. The figures as so modified are as follows:

ESTIMATED AVERAGE COSTS PER ACTIVE CAR-DAY

	1948	1950	1952
	Cents	*Cents*	*Cents*
Cost of freight-car repairs	73.131	80.591	92.591
Deadhead haulage of freight-car repair material	2.117	2.315	2.664
Charges to depreciation of freight cars	43.865	51.379	53.452
Charges account of maintenance and depreciation of shops	6.297	5.942	6.467
Miscellaneous maintenance of equipment accounts	4.901	5.962	6.986
Allocated proportion of general expense	3.339	3.891	4.691
Interest on freight-car value	41.946	50.292	55.508
Interest on value of repair shops	4.093	4.228	4.651
Interest on investment in stock of freight-car repair material	0.524	0.573	0.659
Interest on working capital	0.494	0.545	0.632
Cost of certain taxes	11.369	12.708	13.916
Totals	192.076	218.426	242.217

Additional labor, material, and payroll taxes to reflect increased cost levels as of May 1, 1949, and wages as of January 1, 1949	5.179		
Same as of April 1, 1951		13.134	
Same as of April 1, 1953			1.899
	197.255	231.56	244.116

Car ownership adjusted to car-utilization ratios:

86.12 per cent (1948)—558,428,160 car-days
82.75 per cent (1950)—531,677,250 car-days
86.05 per cent (1952)—559,599,360 car-days

No issue is presented as to the propriety of the charge of $1.75 before April 1, 1951, when the Susquehanna refused to continue the payment of that charge. The table above shows a cost of $2.31 as of that date, and therefore indicates that the charges of $1.75 from that date to April 30, 1952, was not in excess of reasonable compensation. The same conclusion as to the $2 charge in effect for the greater part of 1952 and 1953 is supported by the showing of an average cost of at least $2.42 in those years. The present charge of $2.40, in effect since July 31, 1953, is slightly lower than the cost of approximately $2.44 shown in the table as of April 1, 1953, and we conclude therefore that a charge of $2.40 under present conditions is reasonable compensation.

The Susquehanna in its requested findings suggests that there is a "zone of reasonableness" for per diem charges sufficiently wide to include the amounts for which it seeks approval as not "unjust or unreasonably low or noncompensatory for the periods of their effectiveness, and * * * within the zone of reasonableness." By Section 1(14)(a) we are authorized "to establish * * * the compensation to be paid" as car rental. This wording does not indicate that the authority may be exercised merely by defining the upper or lower limits of a zone of reasonableness, as is usually permitted in respect of transportation rates payable by shippers.

Consequently, our finding below specifies the per diem charges which, on the basis of the facts and circumstances before us, could properly be established under section 1 (14)(a). It necessarily follows that lower charges in our judgment would not be compensatory, either at present or in the past.

We find and declare that the per diem charges of $1.75, $2, and $2.40 were not in excess of reasonable compensation during the periods in which they were effective, and that the latter charge is not in excess of reasonable compensation for present use.

An order discontinuing this proceeding will be entered.

COMMISSIONER ALLDREDGE did not participate in the disposition of this proceeding.

APPENDIX

Intervenors in support of Complainants—The Chesapeake and Ohio Railway Company; Chicago, Rock Island and Pacific Railroad Company; The Delaware and Hudson Railroad Corporation; The Delaware, Lackawanna and Western Railroad Company; Erie Railroad Company; Louisville and Nashville Railroad Company; Minneapolis, St. Paul and Sault Ste. Marie Railroad Company; New York Central Railroad Company; The New York, Chicago and St. Louis Railroad Company; Northern Pacific Railway Company; The Pittsburgh & Shawmut Railroad Company; Southern Pacific Company; Union Pacific Railroad Company; Texas and New Orleans Railroad Company; Western Maryland Railway Company.

Intervenors in support of Defendants—The Ahnapee and Western Railway Company; Alexander Railroad Company; The Atlantic and Danville Railway Company; Bamberger Railroad Company; Bath and Hammondsport Railroad Company; Beaufort and Morehead Railroad Company (A. T. Leary, Lessee); Belfast and Moosehead Lake Railroad Company; Butte, Anaconda & Pacific Railway Company; Charles City Western Railway Company; Chattahoochee Valley Railway Company; Chesapeake Western Railway; Chicago, West Pullman & Southern Railroad Company; City of Prineville Railway; Craig Mountain Railway Company; Detroit and Mackinac Railway Company; Escanaba and Lake Superior Railroad Company; Flemingsburg and Northern Railroad Company; Fort Dodge, Des Moines &

Southern Railway Company; Genesee and Wyoming Railroad Company; Georgia, Ashburn, Sylvester & Camilla Railway Company; The Georgia Northern Railway Company; Hampton & Branchville Railroad Company; High Point, Thomasville & Denton Railroad Company; Howard Terminal Railway; Jerseyville and Eastern Railroad Company; Kentucky & Tennessee Railway; Lackawanna and Wyoming Valley Railroad Company (E. McLain Watters, Trustee); Lake Erie, Franklin & Clarion Railroad Company; Lakeland Railway; Live Oak, Perry & Gulf Railroad Company; Maryland and Pennsylvania Railroad Company; Minneapolis, Northfield and Southern Railway; Morehead and North Fork Railroad Company; The Narragansett Pier Railroad Company, Inc.; Nelson & Albemarle Railway Company; Norwood & St. Lawrence Railroad Company; Oregon & Northwestern Railroad Co.; Oregon Pacific and Eastern Railway Company; Paris and Mt. Pleasant Railroad Co.; Pearl River Valley Railroad Company; Rahway Valley Company (Rahway Valley Company, Lessee); Roscoe, Snyder and Pacific Railway Company; St. Marys Railroad Company; San Francisco and Napa Valley Railroad; The San Luis Central Railroad Company; Santa Maria Valley Railroad Company; Savannah & Atlanta Railway Company; The South Georgia Railway Company; Tennessee, Alabama & Georgia Railway Company; Trona Railway Company; Ventura County Railway Company; Virginia Blue Ridge Railway; Washington and Old Dominion Railroad; Washington, Idaho & Montana Railway Company.

IV. Proposed Report of the Trial Examiner

INTERSTATE COMMERCE COMMISSION

No. 31358

CHICAGO, BURLINGTON & QUINCY RAILROAD COMPANY, ET AL.

v.

NEW YORK, SUSQUEHANNA & WESTERN RAILROAD COMPANY (H. K. NORTON, TRUSTEE) ET AL.

Submitted Decided

Per diem charges of $1.75 and $2 for the use of railroad-owned freight cars when on the lines of rail carriers other than their owners in effect prior to August 1, 1953, found reasonable and a charge of $2.10 found reasonable for present use. Declaratory order entered.

S. R. Brittingham, Jr., R. R. Bongartz, Carson L. Taylor, J. P. Fishwick, F. E. Baukhages, C. C. Howell, E. H. Burgess, D. O. Mathews, Eldon Martin, Edwin C. Matthias, D. S. Wright, B. J. Viviano, Thomas T. Railey, H. Merle Mulloy, J. L. Homire, Seddon G. Boxley, J. T. Suggs, W. C. Plunkett, J. H. Miller, J. L. Rice, R. S. Outlaw, J. H. Wright,

E. J. Zoll, Jr., J. Carter Fort, Jr., Alfred W. Hesse, Jr., Martin A. Meyer, Jr., and *George W. Holmes* for complainánts.

Carl Newton, Granville Whittlesey, W. J. Hickey, J. W. Grady, H. D. Boynton, Richard Jackson, Lawrence Chaffee, William A. Colton, Richard Swan Buell, and *Joseph P. Hawryluk* for defendants.

Hewitt Biaett, J. C. Kauffman, Ross L. Thorfinnson, W. H. Parsons, Prime F. Osborn, III, Thormund A. Miller, M. C. Smith, Jr., Robert D. Brooks, John Colgren, Kemper A. Dobbins, Warren H. Ploeger, W. H. Fitzpatrick, John F. Reilly, Paul F. Robinson, and *Martin L. Cassell* for interveners in support of complainants.

W. J. Hickey, Matthew Crawford, and *Milton Ferguson* for interveners in support of defendants.

REPORT PROPOSED BY HOWARD HOSMER, EXAMINER

The complaint herein was filed September 21, 1953, by 19 of the larger class-1 railroads listed in the footnote.[1] The defendants include among others 5 class-1 railroads: Boston and Maine Railroad; The Long Island Railroad Company (William Wyer, Trustee), (the Long Island); The New York, New Haven and Hartford Railroad Company (the New Haven); New York, Susquehanna & Western Railroad Company (the Susquehanna); and the Rutland Railway Corporation. Six short-line railroads are also defendants: Atlantic & East Carolina Railway Company; East Tennessee and Western North Carolina Railroad Company; St. Johnsbury & LaMoille County Railroad; The New Jersey and New York Railroad Company (Horace Banta, Trustee); and Mississippi & Skuna Valley Railroad Company. The last-named defendant is a class-III railroad; the preceding 5 are class-II lines.

[1] The Atchison, Topeka and Santa Fe Railway Company; Atlantic Coast Line Railroad Company; The Baltimore and Ohio Railroad Company; Chicago & Eastern Illinois Railroad; Chicago, Burlington & Quincy Railroad Company; Chicago, Milwaukee, St. Paul & Pacific Railroad Company; Great Northern Railway Company; Gulf, Mobile & Ohio Railroad Company; Illinois Central Railroad Company; Lehigh Valley Railroad Company; Missouri Pacific Railroad Company (Guy A. Thompson, Trustee); Norfolk and Western Railway Company; The Pennsylvania Railroad Company; Reading Company; The St. Louis-San Francisco Railway Company; Southern Railway Company; The Texas and Pacific Railway Company; The Virginian Railway Company; Wabash Railroad Company.

There are 14 interveners in behalf of the complainants, all of them being class-I railroads. The interveners in behalf of defendants, 57 in number, are railroad carriers principally in classes II and III. All the interveners are listed in the appendix.

The complaint grows out of a disagreement between the complainants and the defendants concerning the reasonableness of per diem charges for the use of railroad-owned freight cars payable by nonowning railroads. In *Alabama, T. & N. R. Co.* v. *Aberdeen & R. R. Co.*, 274 I.C.C. 383, decided July 11, 1949, (hereinafter referred to as the 1949 report), the Commission found that the per diem charge of $1.50 per day then in effect was not shown to be either unreasonably high or unreasonably low. Effective November 1, 1949, that charge was increased to $1.75 by action of members of the Association of American Railroads (hereinafter called the AAR) under procedure described in the 1949 report.

The procedure for establishing per diem charges was considered by division 2 of the Commission in *Association of American Railroads—Agreement*, 277 I.C.C. 413, and approved as conforming to section 5a of the Interstate Commerce Act. The report included the following paragraph:

> Articles XI and XII accord to each subscriber certain individual rights. The former states that the agreement shall not be construed to prevent or limit recourse to this Commission by any subscriber for any

relief (in pending proceedings, or otherwise) accorded by law in respect of any of the matters covered thereby. The latter (article XII) provides that all subscribers shall have the free and unrestrained right to take independent action either before or after any determination arrived at through the procedure provided for in the agreement.

This agreement became effective October 7, 1950. Under the procedure which it set up the per diem charge was increased to $2, effective May 1, 1952, and to $2.40, effective August 1, 1953.

The Susquehanna, which was not a party to the agreement, notified the complainants in March 1951 that after April 1, of that year it would refuse to pay the charge of $1.75 but would settle on a graduated scale ranging from $1.20 to $2, depending on the age of the car. In 1953 it offered to increase that scale to a range between $1.33 and $2.21. The complainants refused those offers, and the car rentals payable by the Susquehanna are now involved in a number of pending lawsuits.

In June 1953 the Boston & Maine, the New Haven, and the Rutland gave notice of their refusal to pay the charge of $2.40 as well as to pay the former $2 charge after July 31, 1954. Later the Boston & Maine offered to pay on a graduated basis or a flat rate of $1.72 per day. The Long Island in August 1953 advised that it was willing to continue paying a $2 charge but would not accept the $2.40

charge. The Atlantic & East Carolina, St. Johnsbury & Lamoille County, New Jersey & New York, and the Barre & Chelsea have followed a similar course. The situation with respect to present payments by defendants other than those here named is not disclosed.

It is alleged in the complaint that, to the extent that the defendants have paid and are paying or offering to pay charges less than those generally in effect as above indicated, "such payments have been, are and would be unjust, unreasonable and noncompensatory, in violation of paragraphs (4), (10) and (11) of section 1 of the Act; and such action by defendants has been, is and would be disruptive of the 'uniform national basis' of handling per diem, which has been deemed necessary by the Commission in order to facilitate 'the performance of orderly transportation service by railroad in the public interest.' *Association of American Railroads—Agreement, supra,* 423." The prayer of the complaint is that—

> the Commission find and declare that the per diem rates of $1.75 and $2, during the period in which these rates were effective, were just, reasonable, and otherwise lawful, that the current per diem rate of $2.40, effective August 1, 1953, is just, reasonable and otherwise lawful, and that the performance of orderly transportation service by railroad in the public interest requires uniform observance of such rates by defendants together with other carriers; and that the Commission grant such other and further relief as may be required in the premises.

The complainants expressly disclaim any intention to invoke the only specific power with respect to per diem which the Commission has, namely by section 1 (14)(a) to establish "the compensation to be paid and other terms of any contract, agreement, or arrangement for the use of any locomotive, car, or other vehicle not owned by the carrier using it (and whether or not owned by another carrier)". Such action would involve the entry of an order, which presumably would continue in effect for the indefinite future and, unless it were vacated or modified, would render the present procedure for dealing with per diem charges inoperative.

In a joint answer to the complaint filed by the Boston & Maine, the New Haven, and certain short-line defendants these parties ask "that the Commission find and determine and fix by order the rate or rates for the use of freight cars to be paid by complainants to defendants and by defendants to complainants." The short-line defendants and interveners request in their briefs that the Commission determine and definitely fix the amount of compensation to be paid by a rail carrier when it uses the freight cars of another, but the briefs of the other defendants are less positive. The New Haven and the Boston & Maine ask for a declaration that the present per diem rate is unlawful and as a maximum should not be more than $1.04 per day if it is to be fixed as a single amount. Alternatively they prefer a graduated scale. The Susquehanna asks principally that the graduated scale which it favors be found not unreasonably low or noncompensatory. The Long Island

and the New Jersey & New York urge that the complaint should be dismissed and assert that the Commission is not empowered to prescribe charges for car hire retroactively. As was suggested at the prehearing conference, it appears that the majority of the parties, except the short lines, prefer that the Commission take action in the nature of a declaratory order, which under section 5(d) of the Administrative Procedure Act it may issue "to terminate a controversy or remove uncertainty." Manifestly there is a controversy here and uncertainty as to the measure of just compensation due complainants from the defendants for the use of cars owned by the former.

With the exception of its action in *Increased Per Diem Charge on Freight Cars*, 268 I.C.C. 659, which was set aside upon judicial review, *Palmer* v. *United States*, 75 F. Supp. 63, the Commission has never undertaken to establish a general basis of per diem charges under its authority in section 1 (14)(a). The present system of rentals in its broad form has been worked out by the railroads themselves. The per diem plan was adopted in 1902 after a mileage system was found to be unsatisfactory for reasons mentioned in *Rules for Car-Hire Settlement*, 160 I.C.C. 369, 375. The charge has been uniform for all types of cars, and up to the time of the present controversy it has applied uniformly to all railroads, subject to the operation of reclaims. In its 1949 report (p. 386) the Commission said:

> For many years the per diem rate has been based on average costs. The daily rental for a car valued at $2,000, for example, is the same as that for a car worth

twice as much. There is no request herein for different per diem rates on freight cars of different ages, sizes, or classes. A carrier which has a foreign railroad car on its rails immediately after midnight pays the rental for that calendar day in the absence of some special agreement. If it receives a car in interchange after midnight and delivers it in interchange before the following midnight, it does not pay any car rental.

Some of the defendants here question the principle of uniformity and introduced evidence in support of their views. These will be discussed before the main issues in the case are considered.

Both the Long Island and the New Jersey & New York, whose lines are partly in the metropolitan area of New York City, perform comparatively short line-hauls in their freight service. The average detention per car in their terminals is high. These defendants believe that the basis of per diem charges should take into account a distinction between items of car-ownership cost attributable to movement use (mileage) and those related to the passage of time. They therefore suggest a basis under which "each using road would pay time costs in proportion to the time that it holds the car and mileage costs in proportion to its own mileage use of the car."

Unless the Commission dismisses the complaint, the Long Island and the New Jersey & New York urge that it—

> (a) undertake to determine true freight car ownership costs * * * (b) make an accurate separation of

> such costs between time and mileage; (c) determine separate average unit costs for time and mileage; and (d) fix separate car hire charges for each user road reflecting the average time and mileage costs for which such road is responsible.

Admittedly such a determination could not be made from the evidence in this case. Apparently it would involve a gigantic statistical undertaking. If by that means a scheme of equitable separate charges for individual user roads could be devised, there would be an increase in the labor now required for settling per diem accounts.

The New Haven and the Boston & Maine suggest a plan of per diem charges under which there would be a variation of rates with respect to owner railroads based on the average age of their cars. The Susquehanna also supports this suggestion. According to the sponsors, this plan "by giving higher rent for new than for old cars would furnish an incentive to car owners to renew the fleet and to get rid of old equipment." The steps necessary to carry out the plan are stated as follows:

> Mr. Glacy's program assumed that in each year the AAR would ascertain for each owning railroad the inventory of its cars; ascertain for each group of cars of each railroad the proper charge per day; and derive for each railroad a composite figure which was the weighted average rate per day for its entire fleet. The AAR would then publish a booklet showing each own-

ing railroad's composite rate, which would be the basis.

This plan, too, would necessitate a complicated statistical operation to ascertain the proper composite figure, and it may well be doubted whether the clerical labor required in computing per diem credits would be as simple as the sponsors believe.

As above indicated, the suggested plans for varying per diem charges could not be put into effect without an extensive investigation either by the Commission or by the AAR. The facts and arguments here presented are not deemed persuasive that plans of this kind are desirable. If the Commission should have a different view, however, there would still be a considerable interim in the future in which a single uniform charge would necessarily have to be applied. Furthermore the issue of reasonableness of the present charge and its immediate predecessors raised in this proceeding must be decided.

There is general agreement that car rentals, whether established by the Commission or otherwise, should be reasonably compensatory and no more, *Palmer* v. *United States*, *supra*, 69. The determination is essentially a problem in cost accounting. The earliest attempt to deal exhaustively with the problem was made 45 years ago by the socalled McCrea commission, composed of 5 railroad presidents. They adopted the principle that the per diem charge should cover (1) repairs, (2) taxes, (3) depreciation, (4) interest on investment, and (5) miscellaneous ex-

pense incidental to ownership. This principle has been generally accepted as valid ever since, but there has been continuing controversy as to how the principle shall be applied. Indeed the members of the McCrea Commission themselves reached three different conclusions on that point.

The principle just referred to serves as a guide for the General Committee of the AAR, which is charged with studying proposals for changes in per diem rates, aided by a subordinate special committee, known as the Subcommittee on Mileage and Per Diem. Costs are allocated to the various categories from expense figures reported to the committees in response to questionnaires sent to car-owning railroads. The General Committee alone decides what proposed changes in the per diem rate shall be recommended to the Board of Directors of the AAR for submission to subscribers to the per diem agreement.

In its 1949 report the Commission discussed the allocations of costs for 1946 presented in support of the per diem charge of $1.50 there in issue. It criticized some of the allocations as too large, but in respect of other important items it made comments which could be interpreted as finding that those items were understated. In an appendix there were shown "averages of such costs as reallocated in the accompanying report" apparently indicating a view that the average cost per active freight car per day was $1.92 in 1947.

It is understandable, therefore, that the complainants lean heavily on the 1949 report, on which they comment in their brief as follows:

> * * * the Commission resolved in favor of the present complainants almost every issue now in dispute, and indicated approval of, if it did not formally prescribe, a formula for the ascertainment of per diem rates which, when applied in this case, establishes the validity of the rates that defendants are here assailing.

If the 1949 report is to be construed as prescribing a formula, the complainants should prevail in the instant case, for that report contains a number of statements highly favorable to their contentions. In the 1949 report, however, the Commission dismissed the complaint in No. 29587, brought by the short lines, which asked the Commission among other things "to promulgate a formula to be employed in the future in determining the lawful compensation to be paid for the use of railroad-owned freight cars." Also it dismissed the complaint in No. 29751, in which six large western lines took the position that the per diem charge of $1.50 was "inadequate, unjust, and noncompensatory." Therefore the soundest interpretation of the 1949 report seems to be that the statements therein were intended to have no significance except as reasons for approving the charge of $1.50 per day.

In this case the complainants seek findings which would approve all per diem charges established after the 1949 report. In each instance the General Committee studied

statistics reported by class 1 railroads in response to questionnaires. Those upon which the charge of $1.75 was based were for 1948, but there was an adjustment to reflect wage rates, material prices, and payroll taxes and other determinable increases up to September 1, 1949. The statistics pertaining to the $2 charge were those for 1950, projected to include cost levels as of April 1951. Full recognition was thus given to the 40-hour week, which was in effect throughout 1950. The present charge of $2.40 was based on figures for 1952. The information for the latter year was received from 121 railroads, having approximately all the freight-car ownership of class 1 railroads. Concerning the latest study, the complainants' principal witness testified that it "came closer to applying the Commission formula [1949 report] than any of its previous studies leading to a per diem adjustment."

Freight car repairs—This is the largest single category of expense included in the per diem charge and amounts to about 40 per cent of the total. Also it is used as a basis of allocating certain other costs.

The basic figures for this item are derived from account 314, Freight Train Cars—Repairs, in the accounting classification. The reported total for 1952 was $586,914,603. To this the General Committee added $24,965,504 for switching home freight cars marked for repairs, and deducted $65,887,034 for costs of car users' repairs to foreign cars damaged by them through improper handling, compensation for foreign cars destroyed on car users' lines,

certain switching costs, and a portion of labor costs of inspection and other service at terminal and junction points. The reasons for these adjustments were stated on pp. 390-1 of the 1949 report. The complainants thus estimate the cost of repairs at 97.836 cents per active car day.

In the 1949 report the Commission found that there should have been a further deduction of the costs incurred by car users for inspection of foreign cars not charged back to car owners. The complainants have not seen fit to consider this deduction as part of what they regard as the Commission's formula, approved or prescribed in the 1949 report. They argue:

> It is technically true that the expense is not one which the owner bears immediately and directly but it is one which the owner bears vicariously and by substitution; and nonowners should not be shielded from the impact of this ownership burden.

Applied to the 1952 study the deduction would amount to only about 5 cents per day, a relatively small figure. Nevertheless Commission's reasons for excluding the item seem sound.

The defendants contend that there should be even larger deductions for the expense of car inspection now included in account 314. Some of the defendants would eliminate all inspection costs on the ground, as stated by one of them, that "inspection is obviously primarily for purposes of operation and safety, and with the primary objective of

preventing breakdowns in transportation on the inspecting line, which is the line which is using the cars." Such a sweeping generalization can not be sustained. The instructions published in connection with the accounting classification direct that "the cost of repairs * * * shall include the cost of inspecting to determine the repairs necessary and * * * the cost of inspecting and testing after repairs have been made * * * to determine whether the repairs have been properly made." The cost witness for the short-line parties in effect conceded that inspection costs of this kind may properly be considered maintenance. If there is to be any segregation of inspection costs as between maintenance and transportation, it should follow an authoritative study.

In the 1949 report the Commission said (p. 391):

> Numerous repairs are applied to freight cars when on the lines of railroads other than their owners, and, except for the relatively few due to defects for which the using line is responsible by reason of improper handling, commonly called no-bill repairs, definite sums published in connection with the freight-car interchange rules may be billed against and collected from the owning railroads. Such amounts are revised from time to time, to correspond with changes in labor and material costs, but as the published revisions lag behind changes in price levels, the actual costs, in a period of rising prices, of supplying materials and applying repairs to foreign cars may, and frequently do, exceed the amounts that may be recovered.

Some of the defendants contend here that losses which they and other carriers incur because of their inability to recoup full costs of these repairs both on foreign per diem cars as well as mileage cars should be deducted from the total car repair costs. It is testified for the Boston & Maine that this deficiency is equivalent to nearly 30 per cent of its charges to account 314, and applying this percentage to aggregate car repair costs of $586,914,603 used in the complainant's study, it suggests the elimination of $175,006,186 from that aggregate. It would be very hazardous to make any such adjustment in the absence of fairly complete information bearing on the matter. Other defendants more cautiously suggest only that the situation should be investigated. This attitude seems to be reflected in the recommendation of the Susquehanna that "there should be segregated and eliminated from ownership cost figures all amounts spent by users for the maintenance of cars which are not recoverable by the user from the owner."

The various defendants introduced four cost str in which the aggregate car-repair figures there shown differ widely. That of the short-line parties shows a total of $498,922,522. The figure in the New Haven study is $457,610,831. Much lower are those of the Boston & Maine, $259,486,694, and of the Susquehanna, $217,158,403. Each of the witnesses who presented these studies is a man of long experience in this field. The wide variations in these figures apparently reflect individual differences in respect of reliance upon conjectural factual data.

Some conjecture of this kind is inescapable because of the comprehensive nature of account 314. It is the largest of the primary operating expense accounts, embracing nearly 10 per cent of total freight expense. It includes "the net loss sustained on account of the destruction of foreign cars" and "amounts paid to others for repairs of freight cars for which the carrier is liable." Among the freight cars covered by the account are cabooses and refrigerator cars. As of November 1, 1953, however, 96.5 per cent of the cars owned by class 1 carriers consisted of box, gondola, hopper, stock, and flat cars, subject to per diem.

The Subcommittee on Mileage and Per Diem in 1951 came to the conclusion that a proper per diem charge could be more readily determined if account 314 could be subdivided and recommended that all the railroads do so beginning with 1952. The Subcommittee found that there was "considerable variation in the practices of various railroads in the charging of inspection costs as between account 314 and account 402." It was of the view that "it would be better if car repairs for cabooses could be eliminated from account 314 and caboose car days eliminated from the freight-car day divisor." The Subcommittee also proposed that there be a separation of repair costs for home cars, foreign cars, and railroad and privately-owned mileage cars, as well as cabooses and a separate showing of cost of classified repairs, running repairs, switching expenses, and credits for sales of scrap. The General Committee disapproved this recommendation because of the additional

expense which would be required for such detailed accounting.

There appears to be good reason for the Commission and the railroads to give careful consideration to the recommendation of the Subcommittee in the interest of removing some of the controversy surrounding this subject. Account 314, as before indicated, includes items of expense which are not related to per diem cars, such as the repairs to cabooses and railroad-owned cars rented on a mileage basis. These expenses should be segregated by special studies currently maintained. However, it is not desirable to delay the decision of this case pending an effort to provide addition data bearing on car repairs. Accordingly, it is concluded that car-repair costs should be determined in the manner specified in the 1949 report.

Taxes—In 1952 the class 1 railroads showed a total investment of $32,698,240,806 in property, material, and supplies, upon which they paid property taxes (personal and real) and other taxes in lieu thereof but excluding State income taxes amounting to $319,221,322, a ratio of 0.976 per cent. That ratio is applied to ledger value of freight cars, undepreciated, and a freight-car repair proportion of ledger value, undepreciated, of shops, enginehouses, etc., producing $56,639,614. To this figure was added $23,354,062 as a proper estimated share of payroll taxes, which makes a total of $79,993,676 for taxes. This is translated into a figure of 14.334 cents per active car day for taxes.

The defendants point out that in some important States no ad valorem taxes are levied on freight cars and make certain other criticisms of the complainants' tax allocations. The Susquehanna suggests that the figure of 14.334 cents "should be reduced by at least 50% pending a country-wide analysis leading to calculations based on accurate comprehensive figures." The Boston & Maine is of opinion that in the light of its experience the property-tax figure of $56,639,614 should be reduced by 70%, making it $16,991,884. The reduction would amount to 7 cents per active car-day.

In the absence of more exact figures the complainants' allocation of this expense appears not to be excessive.

Depreciation—On this subject the complainants say in their brief:

> In the 1948 and 1950 studies, leading to the $1.75 and $2.00 per diem rates, the General Committee used the carriers' aggregate recorded depreciation as the depreciation element of freight car ownership cost. The depreciation item thus reflected freight car value based on original cost. Prior per diem rates had been similarly calculated.
>
> In [the 1949 report] the Commission discussed the contentions of the parties concerning original cost versus replacement value in connection with depreciation and interest return, and its conclusions are reflected in the observation that:

> Carriers who now buy cars must pay prices predicated on present values, and those who rent cars owned by others should expect to pay rentals based on such values.
>
> In conformity with the foregoing statement the Commission computed both depreciation and interest on the basis of replacement value in the formula appended to its report in the prior case.
>
> * * * the General Committee adopted the principle laid down by the Commission, and calculated the annual depreciation charge on the basis of reproduction value. The difference between using original cost and using reproduction value as the depreciation base * * * is the difference between a cost per day of 30.281 cents and 53.598 cents.

The foregoing constitutes the sole justification offered by the complainants for depreciation based on cost of reproduction. They do not undertake to support their position by citation of court decisions or modern accounting practice.

The short-line parties presented as a witness an experienced certified public accountant, who expressed the opinion that depreciation based on cost of reproduction was not in accord with governmental regulations or recognized accounting practice. That view is supported by the general agreement of economists that the purpose of depreciation accounting is not to provide a fund for the replacement of

units of property being retired but to recover the cost of those units in current use.[2]

The holding of the Supreme Court based on a contrary view in *United Railways* v. *West*, 280 U. S. 234, cited in the 1949 report, was expressly overruled in *Federal Power Commission* v. *Hope Natural Gas Co.*, 320 U. S. 591, commonly known as the *Hope* case. The 1949 report is unique among Commission decisions in suggesting the desirability of using reproduction cost as a basis for depreciation. The question was considered exhaustively 18 years before in *Telephone and Railroad Depreciation Charges*, 177 I.C.C. 351, 372-382, shortly after the decision in *United Railways* v. *West, supra.* There the rail carriers urged "that the operating expense resulting from the retirement of a unit of property is not its original cost but rather the cost of replacing it in kind." The Commission rejected that view, and its comments at pp. 377-8 are pertinent here:

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[2] See Barnes-The Economics of Public Utility Regulation, p. 259; Troxel-Economics of Public Utilities, p. 337; Thompson & Smith-Public Utility Economics, p. 330.

The New York Public Service Commission very recently rejected a suggested method "to protect equity investors in utilities against the rigors of inflation, the use of depreciation calculated not upon the basis of cost or investment but in dollars adjusted to the same purchasing power of the dollar originally committed to the enterprise." *Re New York Telephone Co.*, 5 PUR 3rd 33, 46.

See also Hills—The law of Accounting, 54 Col. L. Rev. 1, 20 (January 1954). The second installment of this paper contains the most recent discussion of the point, id. 1049, 1077-8. (November 1954).

> When depreciation accounting is employed, a further and important objection to the cost of replacement or present value method is that retirement and replacement of the unit do not occur when the depreciation charge is made, and may not occur until many years in the future. If depreciation charges, therefore, are made each year on the basis of the current replacement cost or present value, they may prove to be quite out of line with this cost or value at the time when retirement actually takes place. In view of the constant shift in such costs and values this would indeed, normally be the case, with the result that the depreciation reserve would be either too large or too small. No very satisfactory method of adjusting these irregularities has been suggested. It would also be necessary for us to exercise constant supervision over the depreciation charges, for the determination of current replacement cost or present value is so controversial a matter that it could not safely be left to the discretion of the carriers.

The last sentence above quoted is an example of general recognition of the fact that cost of reproduction can only be estimated, and the process is inherently difficult, involving many assumptions which are at least open to question. This is true even though the estimates are based as they are here on data obtained from the Commission's valuation records.

In determining depreciation to be considered in arriving at a proper per diem rate the basis should be ledger value in accordance with the generally accepted accounting theory.

Capital Charges—In connection with this element also the use of cost-of-reproduction is a point of controversy. On this subject the Commission in its 1949 report said: (a. 393)

> An appropriate interest rate, if applied to depreciated ledger cost of freight cars, would not adequately compensate car owners, because such value, averaging $1,092 for freight cars in the service of class 1 railroads at the end of 1946, was 42.3 per cent below their estimated value, averaging $1,891, at that period. Carriers who now buy cars must pay prices predicated on present values, and those who rent cars owned by others should expect to pay rentals based on such values. Inclusion in the per diem rate of an interest charge of 6 per cent on average present value of freight cars, freight repair shops, et cetera, does not appear to be excessive, in view of the fact that a portion of the resulting revenue must be paid out as income taxes.

The complainants are probably justified in asserting that the Commission "held that interest should be computed at 6 per cent on reproduction value," but they do not consider this to be a mandatory requirement. In their brief they say:

> **In connection with the $2.40 rate the General Committee's averaging method produced an interest on value item for freight cars of 43.588 cents, as against 31.516 cents on depreciated ledger value alone. If the General Committee had followed the Commission's decision and used depreciated reproduction value, the amount included in the per diem computation for interest on freight car value would have been 55.660 cents, and the current rate would be substantially in excess of $2.40.**

The "averaging method" above mentioned produced an investment base which was the average of depreciated cost of reproduction and depreciated ledger value. To this a 6-per cent rate of return was applied. The theory followed in determining this base is essentially the same as that of "fair value" which flourished about 25 years ago but has lost most of its significance since the *Hope* case.[3]

It is true, as complainants say, that the Commission's right to recognize reproduction value is not to be questioned, but the 1949 report in its extreme reliance on present value may properly be characterized as anomalous. Long before the *Hope* case, the Commission in 1927 carefully pointed out the weaknesses of the cost-of-reproduction basis in *Excess Income of St. Louis & O'Fallon Ry. Co.*, 124 I.C.C. 3, 28-37. Later in *Petroleum Rail Shippers' Assn. v. Alton & S.R.*, 243 I.C.C. 589, 663, the Commission de-

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[3] See "The *Hope* Case and Public Utility Valuation in the States (Rose), 54 Col. L. Rev. 188 (May 1954).

termined the value of two pipeline carriers on the basis of original cost less depreciation instead of the lower cost of reproduction. In the general rate-increase cases since 1946 the Commission has adhered to original cost as the principal element in the rate base, *Increased Freight Rates,* 1947, 270 I.C.C. 403, 436; *Increased Freight,* 1951, 284 I.C.C. 589, 607. Even more pertinent here is the decision in *New York, S. & W. R. Co. Abandonment,* 275 I.C.C. 10, in which there was an issue of just compensation to the Susquehanna for transportation service which it performed for the New York Central. At p. 16 of that report the Commission said:

> The Susquehanna maintains that reproduction cost at present-day prices, less depreciation, provides a more fair and equitable basis for determining a fair return on value than original cost less accrued depreciation. The Central insists that the latter factors should be used * * * We likewise consider original cost less depreciation as the most suitable base for the purpose of this case. In any future revisions of the cost study, such base could be quickly and inexpensively determined.

The last sentence above quoted recognizes the fact already pointed out that cost of reproduction is an unstable and indefinite base not readily ascertainable. This objection is sufficiently forceful in itself to justify the sole use of depreciated ledger value as an investment base for present purposes without considering other criticisms of the cost-of-reproduction basis which have caused it to be discredited in the past 10 years.

The choice of a percentage figure to be applied to the investment base must rest necessarily on judgment in a field which has been a battleground of controversy for about half a century. Although all the defendants take much the same position as the Boston & Maine, which asserts that "it would be improper to include anything in the rent base beyond the costs of financing such property—in this instance the interest burden upon a car owner arising out of his acquisition and ownership of a freight car," the only ones making definite recommendations as to a rate of return are the New Haven, the Boston & Maine, and the Susquehanna. The first-named suggests 6 per cent based on ledger value, but the other two say it should be about 4.6 per cent of that value. The latter figure is the result of an averaging process, reflecting among other things the average interest rate of 2.39 per cent on outstanding equipment-trust obligations.

In urging that "the General Committee's formula conservatively understates the legally allowable charge for depreciation and interest return as elements of ownership cost", the complainants stress "risk of ownership" and "burden of replacement" incurred by the car-owning carriers and hint at danger to the national economy "if railroads which have heretofore been willing to sink capital in freight cars should decide that in view of high replacement costs prudence no longer permitted them to contribute their part to the national car fleet, but that they should become car renters rather than car owners."

An intervener, the Chesapeake and Ohio Railway Company, which owns a large number of cars and is consequently one of the principal per diem credit railroads is more specific. It states:

> If the railroads in general, and the Chesapeake and Ohio in particular, are to own the number of cars required by the national economy, the per diem rate must provide adequate compensation after income taxes. If the per diem rate provided a realistic rate of return after income taxes, the railroads, including the Chesapeake and Ohio, would own a larger number of cars and could, in fact, justify increasing rather than reducing their car ownership.

This intervener therefore believes that, far from being reduced, "the prevailing per diem rate of $2.40 per car per day is at least 97 cents too low and should be increased." The further expansion of the 97-cent figure which it suggests would be accomplished by adjustment of the car-day divisor to be discussed later.

Argument over investment base and percentage rate of return should not obscure the practical point involved, which is the number of dollars available by way of rental to a carrier which makes an investment in freight cars for joint use in nationwide transportation service. It seems clear that the car-owning carrier is entitled to a return larger than one based solely on cost of money measured by current interest rates, for in acquiring cars it acts somewhat as an entrepreneur. It must assume the burden of planning and financing the new equipment in the light of

an uncertain demand for cars in general or those of a particular size and type due to unpredictable factors affecting the outlook for rail transportation. In other words, it is not disputed that the per diem charge should take some account of what are termed incentive and risk, but the problem of proper allowance for this consideration is difficult. The appropriate place for such an element, it is believed, is in the rate of return without dividing it between that item and the depreciation charge. Also it seems that the defendants are right that the incentive to build new cars will have more force if rate of return is based on original cost.

Another complication has to do with the impact of income taxes. At a time when such taxes were comparatively trivial, the Supreme Court held that the fairness of a return to a utility should be determined on the basis of what it had left after paying income taxes. The validity of this principle is subject to doubt in the present era of high income taxes,[4] but the Commission gave some weight to income tax liability in the 1949 report.

The six-per cent return on depreciated reproduction value, strongly suggested as proper in that report, was equivalent to a return of approximately 10.6 per cent on depreciated original cost. This return, as the Commission pointed out, would be reduced by income taxes. In the instant case it is concluded that a return of 10 per cent

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[4] In Justice Douglas's dissenting opinion in *Vinson* v. *Washington Gas Co.*, 321 U. S. 489, he said: "It is self-evident that the ability to pass present wartime income taxes on to others is a remarkable privilege indeed."

on original cost of freight cars less depreciation would be fair. This would produce a greater amount of money than the allocation for interest in the complainants' studies, but the excess would be much less than the reduction in the allocation for depreciation recommended in this report. Thus the total amount allocated for depreciation on freight cars and interest on the value thereof in complainants' 1952 study is $542,366,675. The corresponding allocation upon the basis here proposed is $462,120,718. On the basis suggested in the 1949 report the allocation for these items would be $609,736,258.

In this report the return on investment in shops, engine-houses, power plants, etc., is based on 6 per cent of depreciated ledger value. This item is relatively unimportant.

The Car-Day Divisor—For reasons which are well-known it is generally agreed that surplus and unserviceable cars should be excluded in computing average costs per car day. However, since per diem charges are established for future application, the extent of that exclusion necessarily rests upon an informed guess as to the aggregate number of freight cars which the railroads will own in an indefinite future period, the number which will be unserviceable, and the number which will be idle because of insufficient traffic for their full utilization. The last element, which is closely related to fluctuations in the business cycle, is particularly speculative. Hence the basis of estimating the percentage of active car-days has always been a subject of wide disagreement. The Commission devoted three pages of its 1949 report to this question, and following paragraph on p. 389 indicates its conclusions:

> The per diem rate could be revised upward and downward periodically to conform to annual fluctuations in the number of active cars, and if based on the approximate costs of ownership and maintenance and active cars for a designated recent year it could not be said to be unreasonable. Or the rate could be determined by the use of an active-car ratio based, from time to time, on the average number of active cars in use over a representative period of years, and, if predicated on the approximate costs of ownership and maintenance for a designated recent year, the rate so fixed could not be said to be unreasonable. Stated differently, there is a rather wide zone of reasonableness within which the carriers may establish a lawful per diem rate. The evidence is persuasive that an active-car divisor reflecting average age, now approximating 20 years, of freight cars in service, and covering representative periods of both heavy and light traffic, would produce more accurate results than a period of 5, 10, or 15 years.

It does not appear that theretofore the railroads had ever considered using a period as long as 20 years for this purpose. In the studies which the AAR presented in connection with the 1949 decision a 10-year period, 1936-1945, was used, and the ratio so arrived at was 86.15 per cent. The 20-year period in the 1949 report covered 1927-1946 and produced a ratio of 80 per cent, the ratio used by the Commission in its "reallocated" costs, which as before shown, were higher than those relied on by the AAR.

Notwithstanding the fact that the Commission's conclusions with respect to the car-utilization ratio were of much potential value to the car-owning railroads, they were not immediately adopted. In the studies which led to the $1.75 charge a period of 15 years, 1934-1948, was used to arrive at a ratio of 86.12 per cent. Originally in the next studies relating to the $2 charge the 15-year period, 1936-1950, was used, and the resulting ratio was 89.13 per cent. However, apparently the General Committee was of the view that due deference to the Commission's views made it advisable to use the 20 years 1931-1950 and thereby reduce the ratio to 82.75 per cent, incidentally increasing the estimated cost by about 15 or 16 cents per day. In the studies on which the present charge was based a 20-year period, 1933-1952, was used, giving a percentage ratio of 86.05 per cent.

In contrast to the ratios above shown, 86.12, 82.75, and 86.05 per cent, are the following actual ratios for the years shown:

Year	*Per cent*
1949	90.39
1950	91.34
1951	94.27
1952	93.59

If the Commission's observations concerning the 20-year period were intended as a general principle for future guidance of the railroads, the present proceeding affords an appropriate opportunity for further consideration of the question. The period gives undeserved weight to condi-

tions in years prior to 1941 which were in a wholly different economic era from that of succeeding years.

For the period from 1933 to 1940, inclusive, the average annual ownership of cars by class 1 railroads was 1,806,065. Because of depressed industrial activity there were large numbers of surplus cars, and the percentage of unserviceability ranged from 8.8 to 15. The car-utilization ratio consequently ranged from 63.98 in 1933 to 84.16 in 1940.

On the other hand, in the years from 1941 to 1952, inclusive, the class 1 railroads' annual ownership of cars averaged 1,738,696. Those carriers were able to carry the heavy traffic of the war and post-war periods because of the greater average capacity of the cars increased train speeds and other means of greater efficiency, including a reduction in percentage of unserviceability to a range between 2.7 and 6.9. Car surpluses after 1940 were negligible in comparison with those of the earlier period.[5] The car-utilization ratio, therefore, between 1941 and 1952 ranged between 90.39 and 96.67. In 1952, the latest year for which figures are to be found in the record, the ratio was 93.59, as before shown. Although the ratio undoubtedly declined in 1953 and 1954, it is doubted whether the

5 Complainants show that maximum freight-car surpluses in 1933-1940 ranged from 190,370 on March 14, 1940 to 691,587 on January 31, 1933. Minimum surpluses in the same period ranged from 64,299 on October 14, 1939 to 385,137 on October 31, 1933. In the period 1941-1952 maximum surpluses ranged from 23,416 on October 20, 1945 to 207,627 on November 5, 1949. Minimum surpluses ranged from 673 on October 23, 1948 to 38,511 on October 4, 1941.

figure has fallen below 90. If so, supplementary figures may be furnished before submission of the case.

The mere fact that freight cars have an average life of about 20 years affords little or no ground for assuming that their probable utilization in any given future year will be the same as that for the average of the past 20 years. There is no reason to believe that economic cycles are so marked.

If the 20-year period is adopted as a permanent yardstick, the statistics for years from 1941 to 1952 will continue to have a varying influence until 1971. Within that future time there may well be changes which will cause the 1941-1952 period to be regarded as abnormal. By 1960 when the favorable influence of the prewar years will have entirely disappeared there may be less satisfaction with the 20-year yardstick.

For the reasons above indicated it is here concluded that that yardstick should be discarded. The proposed findings therefore reflect a car-utilization ratio of 90 per cent.

Conclusions—In accordance with the views before expressed the figures submitted by the complainants have been modified in the following respects: (1) The item for freight-car repairs and the allocations based thereon are treated in the same manner as they were in the 1949 report. (2) Depreciation for freight cars and shops, enginehouses, power plants etc., is based on undepreciated ledger values. (3) Return on investment is based on 10 per cent of depreciated ledger value. (4) Return on investment in shops, enginehouses, power plants, etc., is based on 6 per cent of depreciated ledger value. (5) The car-day divisor is based

on a car-utilization ratio of 90 per cent. The figures as so modified are as follows:

ESTIMATED AVERAGE COSTS PER ACTIVE CAR-DAY[6]

	1948	1950	1952
	Cents	*Cents*	*Cents*
Cost of freight-car repairs	70.01	74.06	88.42
Deadhead haulage of freight-car repair material	2.03	2.13	2.54
Charges to depreciation of freight cars	24.28	26.86	28.84
Charges account of maintenance and depreciation of shops	6.03	5.46	6.18
Miscellaneous maintenance of equipment accounts	4.69	5.48	6.67
Allocated proportion of general expense	3.20	3.58	4.48
Interest on freight-car value	39.46	41.19	50.03
Interest on value of repair shops	2.24	2.29	2.30
Interest on investment in stock of freight-car repair material	0.50	0.53	0.63
Interest on working capital	0.47	0.50	0.60
Cost of certain taxes	10.89	11.68	13.29
Totals	163.80	173.76	203.98

[6] The working papers underlying these computations are available for inspection in the office of the Cost Finding Section of the Commission's Bureau of Accounts Cost Finding and Valuation.

Additional labor, material and payroll taxes to reflect increased cost levels as of May 1, 1949 and wages of January 1, 1949	4.96		
Same as of April 1, 1951		12.07	
Same as of April 1, 1953			1.81
	168.76	185.83	205.78

Car ownership adjusted to car utilization ratio of 90 per cent:

1948—583,286,368 car days
1950—578,535,476 " "
1952—585,970,978 " "

As before stated, the Susquehanna refused to pay the charge of $1.75 after April 1, 1951, and it is therefore unnecessary to consider whether the charge was unreasonable before that date. The table above shows a cost of $1.8583 as of April 1, 1951, and therefore indicates that the charge of $1.75 from that date to April 30, 1952, was not unreasonable. Similarly, the table indicates that the average cost in 1952 and 1953 was at least $2.0398, which was slightly higher than the charge of $2 in effect during the greater part of those years. The present charge of $2.40 is considerably higher than the cost of approximately $2.06 shown in the table, and it is therefore concluded that a reasonable charge under present conditions would be $2.10.

The Susquehanna in its requested findings suggests that there is a "zone of reasonableness" sufficiently wide to include the amounts for which it seeks approval as not "unjust or unreasonably low or noncompensatory for the periods of their effectiveness, and were within the zone of reasonableness. Although the Commission at p. 389 of the 1949 report said that "there is a rather wide zone of reasonableness within which the carriers may establish a lawful per diem rate," the statutory authority of the Commission over per diem rates is not so worded as to indicate that the authority may be exercised merely by defining the upper or lower limits of a zone of reasonableness, as in the case of freight rates.

The Commission should find and declare that the per diem charges of $1.75 *and* $2 *were reasonable during the periods in which they were effective and that a reasonable charge for present use would be* $2.10.

A declaratory order should be entered.

APPENDIX

Interveners in support of Complainants—The Chesapeake and Ohio Railway Company; Chicago, Rock Island and Pacific Railroad Company; The Delaware and Hudson Railroad Corporation; the Delaware, Lackawanna and Western Railroad Company; Erie Railroad Company; Louisville and Nashville Railroad Company; Minneapolis, St. Paul and Sault Ste. Marie Railroad Company; New York Central Railroad Company; The New York, Chicago and St. Louis Railroad Company; Northern Pacific Railroad Company; Southern Pacific Company; Union Pacific Railroad Company; Texas and New Orleans Railroad Company; Western Maryland Railway Company.

Interveners in support of Defendants—The Ahnapee and Western Railway Company; Alexander Railroad Company; The Atlantic and Danville Railway Company; Bamberger Railroad Company; Bath and Hammondsport Railroad Company; Beaufort and Morehead Railroad Company (A. T. Leary, Lessee); Belfast and Moosehead Lake Railroad Company; Butte, Anaconda & Pacific Railway Company; Charles City Western Railway Company; Chattahoochee Valley Railway Company; Chesapeake Western Railway; Chicago, West Pullman & Southern Railroad Company; City of Prineville Railway; Craig Mountain Railway Company; Detroit and Mackinac Railway Company; Escanaba and Lake Superior Railroad Company; Flemingsburg and Northern Railroad Company; Fort Dodge, Des Moines & Southern Railway Company; Genesee and Wyoming Rail-

road Company; Georgia, Ashburn, Sylvester & Camilla Railway Company; The Georgia Northern Railway Company; Hampton & Branchville Railroad Company; High Point, Thomasville & Denton Railroad Company; Howard Terminal Railway; Jerseyville & Eastern Railroad Company; Kentucky and Tennessee Railway; Lackawanna and Wyoming Valley Railroad Company (E. McLain Watters, Trustee); Lake Erie, Franklin & Clarion Railroad Company; Lakeland Railway; Live Oak, Perry & Gulf Railroad Company; Maryland and Pennsylvania Railroad Company; Minneapolis, Northfield and Southern Railway; Morehead and North Fork Railroad Company; The Narragansett Pier Railroad Company, Inc.; Nelson & Albemarle Railway Company; Norwood & St. Lawrence Railroad Company; Oregon & Northwestern Railroad Co.; Oregon Pacific and Eastern Railway Company; Paris and Mt. Pleasant Railroad Co.; Pearl River Valley Railroad Company; The Pittsburg & Shawmut Railroad Company; Rahway Valley Company (Rahway Valley Company, Lessee); Roscoe, Snyder and Pacific Railway Company; St. Marys Railroad Company; San Francisco and Napa Valley Railroad; The San Luis Central Railroad Company; Santa Maria Valley Railroad Company; Savannah & Atlanta Railway Company; The South Georgia Railway Company; Tennessee, Alabama & Georgia Railway Company; Trona Railway Company; Ventura County Railway Company; Virginia Blue Ridge Railway; Washington and Old Dominion Railroad; Washington, Idaho & Montana Railway Company.

Order of the Interstate Commerce Commission

ORDER

At a General Session of the INTERSTATE COMMERCE COMMISSION, held at its office in Washington, D. C., on the 17th day of October, A. D. 1955.

No. 31358

CHICAGO, BURLINGTON & QUINCY RAILROAD COMPANY ET AL.
NEW YORK, SUSQUEHANNA & WESTERN RAILROAD COMPANY ET AL.

This proceeding being at issue upon complaint and answers on file, and having been duly heard and submitted by the parties, and full investigation of the matters and things involved having been made, and the Commission having, on the date hereof, made and filed a report containing its findings of fact and conclusions thereon, which report is hereby referred to and made a part hereof:

It is ordered, That this proceeding be, and it is hereby, discontinued.

By the Commission.

HAROLD D. McCOY,
Secretary

(SEAL).